

Message Text

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ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 AID-05 CIAE-00
EB-08 FRB-01 INR-07 NSAE-00 USIA-15 TRSE-00
XMB-04 OPIC-06 SP-02 LAB-04 SIL-01 OMB-01 NSC-05
SS-15 STR-04 CEA-01 PA-02 PRS-01 EURE-00 AGRE-00
FEA-01 ITC-01 /129 W
-----292142Z 034104 /66

P R 292151Z MAR 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC PRIORITY 2084
TREASURY DEPT WASHDC PRIORITY
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DEPARTMENT PASS FEDERAL RESERVE BOARD

TREASURY FOR DONALD E. SYVRUD, OASIA

E.O. 11652: N/A
TAGS: ECON, UK
SUBJECT: MAJOR FISCAL ELEMENTS IN THE CHANCELLOR'S
MARCH 29 BUDGET

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SUMMARY: A SHIFT FROM INCOME TO EXPENDITURE TAXATION
COUPLED WITH A CARROT AND STICK APPROACH TO ORGANIZED
LABOR TO ACHIEVE A FURTHER YEAR OF WAGE RESTRAINT LIE AT
THE HEART OF THE CHANCELLOR'S BUDGET. INCOME TAX REDUC-
TIONS OF 2.3 BILLION POUNDS TAILORED LARGELY TO BENEFIT
AVERAGE TAX PAYERS AND OFFSET BY AN 0.8 BILLION POUND EX-
CISE TAX INCREASE LARGELY AFFECTING MOTORISTS AND SMOKERS

PRODUCE A 1.5 BILLION POUND NET TAX REDUCTION. NEARLY A BILLION POUNDS OF THIS IS CONDITIONED ON THE CONCLUSION OF A SATISFACTORY ALTHOUGH UNSPECIFIED THIRD YEAR INCOMES POLICY AGREEMENT. HOWEVER. SOME 400 MILLION POUNDS IN EMPLOYMENT SUBSIDIES, TRAINING PROGRAMS AND CONSTRUCTION MEASURES AIMED AT PRESERVING OR CREATING 150 TO 200 THOUSAND JOBS CAN BE SEEN AS A FURTHER INDUCEMENT TO ORGANIZED LABOR. THIS MESSAGE OUTLINES THE PRINCIPAL TAX CHANGES AND MEASURES ANNOUNCED BY THE CHANCELLOR. END SUMMARY.

1. UNCONDITIONAL INCOME TAX CHANGES.

THESE TOTAL 1.35 BILLION POUNDS AND ARE LARGELY ACHIEVED THROUGH INCREASES IN PERSONAL ALLOWANCES AND RAISING THE INCOME BANDS ON WHICH MARGINAL TAX RATES ARE ASSESSED. ACCORDING TO THE CHANCELLOR, THEY ARE DESIGNED TO STRENGTHEN THE INCENTIVE TO WORK THROUGHOUT THE ECONOMY. WHILE THE MAIN IMPACT OF THE ANNOUNCED INCREASES IN PERSONAL ALLOWANCES WILL BENEFIT THOSE AT THE LOWER END OF THE INCOME SCALE, TAXPAYERS AT ALL INCOME LEVELS WILL BENEFIT FROM THEM. WITH REGARD TO LOWERING THE CURRENT BASIC INCOME TAX RATE FROM 35 PERCENT TO 25 PERCENT, THE CHANCELLOR SAID THIS WOULD BE TOO EXPENSIVE AND PROVIDE SPECIAL BENEFIT TO A RELATIVE FEW. HOWEVER, TO PREVENT INCREASINGLY LARGE NUMBERS OF TAXPAYERS BEING PUSHED INTO HIGHER TAX BRACKETS BY THE IMPACT OF INFLATION ON EARNINGS. THE CHANCELLOR INCREASED THE THRESHOLD OF THE FIRST HIGHER TAX RATE (40 PERCENT) FROM 5,000 TO 6,000 POUNDS. ABOVE THIS LEVEL, PROGRESSIVELY LESS GENEROUS INCREASES IN THE THRESHOLD WERE ANNOUNCED. FOR UNCLASSIFIED

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EXAMPLE, AT THE HIGHEST MARGINAL TAX RATE (83 PERCENT), THE THRESHOLD WAS RAISED FROM 20,000 TO 21,000 POUNDS, A 5 PERCENT INCREASE COMPARED WITH 20 PERCENT AT THE 35 PERCENT LEVEL.

2. CONDITIONAL INCOME TAX RELIEF

THE CHANCELLOR PROMISED A FURTHER 960 MILLION POUND REDUCTION IN INCOME TAXES GIVEN "A SATISFACTORY AGREEMENT ON A NEW PAY POLICY." THE REDUCTION WOULD BE ACHIEVED BY LOWERING THE BASIC INCOME TAX RATE FROM 35 TO 33 PERCENT. ACCORDING TO THE CHANCELLOR, "THIS WILL BE A SPECIAL ADVANTAGE TO PEOPLE ON UP TO TWICE AVERAGE EARNINGS, WITH THE BIGGEST PROPORTIONATE BENEFIT GOING TO THE HIGHLY SKILLED WORKER." UNLIKE LAST YEAR THE CHANCELLOR DID NOT COMMIT HIMSELF TO INTRODUCING THIS AT A SPECIFIC TIME. RATHER, HE SAID, "I SHALL MOVE AN AMENDMENT PROPOSING A REDUCTION IN THE BASIC RATE AT THE APPROPRIATE TIME AND IN THE LIGHT OF THE PAY AGREEMENT."

3. INDIRECT TAXATION.

TO THE SURPRISE OF SOME, THE CHANCELLOR REFUSED TO INCREASE VALUE ADDED TAXATION ON THE GROUNDS THAT IT WOULD MAKE IT HARDER TO REDUCE THE RATE OF INFLATION. RATHER, HE CHOSE TO CONFINE INDIRECT TAX INCREASES TO TOBACCO, GASOLINE, HEAVY FUEL OIL, AND VEHICLE LICENSE

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FEA-01 ITC-01 /129 W

-----292143Z 034288 /66

P R 292151Z MAR 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 2085

TREASURY DEPT WASHDC PRIORITY

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FEES. PETROLEUM-RELATED TAXES WERE INCREASED BECAUSE OF THE NEED TO CONSERVE ENERGY WHILE THE INCREASE IN TOBACCO DUTIES WAS JUSTIFIED ON HEALTH GROUNDS. THESE TAX CHANGES WERE DESIGNED TO INCREASE REVENUES BY 811 MILLION POUNDS

WITH ALL BUT 140 MILLION OF THAT COMING FROM THE ENERGY-RELATED EXCISE TAX INCREASES. WHILE THESE INCREASES, WHICH INCLUDE A 5 PENCE (8.5 CENTS) PER GALLON ON GASOLINE
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WILL HIT MOTORISTS, PARTICULARLY COMMUTERS, THE CHANCELLOR MAY WELL HAVE CONCLUDED THAT RELATIVELY FEWER LABOR VOTERS WILL BE AFFECTED BY THE RISES.

OTHER TAX CHANGES.

THE CHANCELLOR DID NOT ANNOUNCE ANY CHANGES IN CORPORATE INCOME TAX LEVELS. HOWEVER, HE DID RAISE THE PROFIT LIMIT FOR THE PREFERENTIAL RATE OF CORPORATION TAX FOR SMALL FIRMS FROM 30 TO 40,000 POUNDS WITH THE LIMIT FOR MARGINAL RELIEF BEING INCREASED TO 65,000 POUNDS FROM ITS CURRENT 50,000. WITH REGARD TO CAPITAL GAINS TAXATION, THE CHANCELLOR MENTIONED IMPROVED TAX RELIEF WITH REGARD TO THE TRANSFER OF AN OVERSEAS BRANCH TO A SEPARATE NON-RESIDENT COMPANY. HE ALSO ANNOUNCED HIS INTENT TO MODIFY RULES APPLYING TO MERGERS AND REORGANIZATIONS.

OF POTENTIAL SIGNIFICANCE TO OIL COMPANIES, THE CHANCELLOR ANNOUNCED HIS INTENT TO BEGIN CONSULTATIONS WITH THE COMPANIES CONCERNED ABOUT RESTRICTING "UNILATERAL RELIEF OR CERTAIN TAXES PAID BY OIL COMPANIES TO GOVERNMENTS OF OIL-PRODUCING COUNTRIES." AS U.S. OIL COMPANIES ARE CERTAIN TO BE AMONG THOSE CONSULTED, THE EMBASSY WILL TRY TO OBTAIN FURTHER DETAILS OF THE CHANCELLOR'S PROPOSALS.

4. EMPLOYMENT MEASURES

TO MAKE FURTHER RESOURCES AVAILABLE FOR THE REDUCTION OF UNEMPLOYMENT, THE CHANCELLOR ANNOUNCED A SERIES OF ADDITIONAL MEASURES WHOSE GROSS COST OVER THE NEXT TWO YEARS IS ESTIMATED AT 400 MILLION POUNDS AND WHICH ARE INTENDED TO CREATE OR PRESERVE 150 TO 200,000 JOBS. THE TEMPORARY EMPLOYMENT SUBSIDY DUE TO EXPIRE NEXT MONTH WILL BE EXTENDED THROUGH MARCH 1978 WITH FIRMS NOW RECEIVING THE SUBSIDY BECOMING ELIGIBLE FOR PAYMENTS FOR A FURTHER 18 MONTHS AT RATES OF 10 POUNDS PER EMPLOYEE PER WEEK. THE CHANCELLOR THEN ANNOUNCED FOUR NEW THOUGH SMALL-SCALE SCHEMES:

1 - SELECTIVE JOB INTRODUCTION SCHEME. THIS WILL
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PROVIDE EMPLOYERS WITH 30 POUNDS PER WEEK FOR A TRIAL PERIOD OF SIX WEEKS IF THEY HIRE DISABLED PEOPLE ON A TRIAL BASIS.

2 - A SPECIAL PROGRAM TO TRAIN MATHEMATICS TEACHERS.

3 - SPECIAL DEVELOPMENT AREA SUBSIDY. FIRMS IN
SPECIAL DEVELOPMENT AREAS EMPLOYING LESS THAN
50 PEOPLE WILL BE ELIGIBLE FOR A WEEKLY SUBSIDY
OF 20 POUNDS PER WEEK FOR A SIX-MONTH PERIOD FOR
EACH ADDITIONAL EMPLOYEE HIRED.

4 - A PROGRAM TO HELP THE LONG-TERM UNEMPLOYED.

THESE SCHEMES ARE ALL OF A PILOT NATURE AND FULLER DE-
TAILS WILL BE ANNOUNCED IN COMING WEEKS.

FINALLY. THE CHANCELLOR ANNOUNCED THAT 100 MILLION
POUNDS FROM THE CONTINGENCY RESERVE WOULD BE ALLOCATED TO
CONSTRUCTION PROJECTS IN INNER CITY AREAS. THIS IS AIMED
AT STIMULATING DEMAND IN AN INDUSTRY WHICH HAS BEEN HARD
HIT BY DEEP CUTS IN PUBLIC INVESTMENT EXPENDITURE. ITS
INCLUSION IN THE BUDGET MESSAGE IS A TACIT ADMISSION BY
THE CHANCELLOR OF THE NEGATIVE IMPACT OF THESE CUTS ON
THE CONSTRUCTION INDUSTRY.

THE FOLLOWING TABLE PROVIDES THE CHANCELLOR'S ES-
TIMATES OF THE INITIAL AND LONGER-TERM REVENUE EFFECTS
OF THE TAX CHANGES ANNOUNCED IN THE BUDGET.

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FEA-01 ITC-01 /129 W

-----292141Z 034285 /66

P R 292151Z MAR 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 2086

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FORECAST EFFECTS OF CHANGES IN TAXATION

THE EFFECTS SHOWN ARE DIRECT EFFECTS, I.E., THE DIFFERENCE BETWEEN THE YIELDS OF PRE-BUDGET AND POST-BUDGET TAX RATES AT THE SAME LEVELS OF INCOME AND ACTIVITY. THE EXPENDITURE TAX FIGURES DO, HOWEVER, ALLOW FOR THE EFFECTS OF RELATIVE PRICE CHANGES ON THE COMPOSITION OF CONSUMER'S EXPENDITURE.

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POUNDS MILLIONS FORECAST FOR 1977-78 FORECAST FOR A FULL YEAR

INCOME TAX

INCOME IN SINGLE ALLOWANCE BY		
70 POUNDS AND IN MARRIED		
ALLOWANCE BY 140 POUNDS	-720	-901
INCREASE IN ADDITIONAL		
PERSONAL ALLOWANCE BY		
70 POUNDS	- 7	- 9
INCREASE IN AGE ALLOW-		
ANCE BY 70 POUNDS (SINGLE)		
AND 140 POUNDS (MARRIED)	- 49	- 60
EXTENSION OF BASIC RATE		
BAND TO 6,000 POUNDS	- 71	- 90
CHANGES IN HIGHER RATE BANDS	- 93	-185
REDUCTION OF 2 P IN BASIC		
RATE (CONDITIONAL ON PAY		
AGREEMENT)	-797	-960
INCREASE IN INVESTMENT IN-		
COME SURCHARGE THRESHOLDS	- 5	- 45
INCREASE IN RETIREMENT AN-		
NUTY RELIEF CEILING	- 5	- 12
INCREASE IN EXEMPTION LIMIT		
FOR SAVINGS BANK INTEREST	NEGLIGIBLE	- 1
CHANGE IN TREATMENT OF		
FOREIGN EARNINGS	- 20	- 30
CHANGE IN TREATMENT OF		
ANNUITIES	2	-

CORPORATION TAX

DECREASE IN RATE OF ADVANCE

CORPORATION TAX TO 33/67 OF
THE AMOUNT OF THE DIVIDEND
(CONDITIONAL ON PAY AGREE-
MENT - 54 -
INCREASE IN LIMIT FOR SMALL
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COMPANY RELIEF	- 11	- 20
TOTAL	-1,830	-2,313

VALUE ADDED TAX

ALTERATIONS IN REVENUE

DUTY RATES	25	35
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AMENDMENTS TO VALUE ADDED

TAX LEGISLATION	NEGLIGIBLE	NEGLIGIBLE
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REVENUE DUTIES

CONSOLIDATION OF SURCHARGE
ON ALCOHOLIC DRINK AND

TOBACCO DUTIES	NEGLIGIBLE	NEGLIGIBLE
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INCREASE IN RATE OF ROAD

FUEL DUTY	275	275
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INCREASE IN EFFECTIVE RATE
OF DUTY ON REBATABLE OIL

	150	150
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INCREASE IN TOBACCO PRODUCTS

DUTY	125	140
TOTAL	575	600

VEHICLE EXCISE DUTY

INCREASE IN RATES	211	211
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NATIONAL INSURANCE SURCHARGE

RELIEF FOR CHARITIES	- 5	- 5
TOTAL	-1,049	-1,507

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: GOVERNMENT REFORM, GOVERNMENT BUDGET, ECONOMIC CONDITIONS
Control Number: n/a
Copy: SINGLE
Sent Date: 29-Mar-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment:
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Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977LONDON05181
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D770107-1064
Format: TEL
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770312/aaaaajtg.tel
Line Count: 368
Litigation Code IDs:
Litigation Codes:
Litigation History: Hold (001 Tobacco) added on 4/16/2009 3:39:00 PM by WASHDCMcGoldRJ, Hold (001 Tobacco) removed on 4/16/2009 3:45:07 PM by WASHDCMcGoldRJ (Litigation Hold Lifted)
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: ceaa01b0-c288-dd11-92da-001cc4696bcc
Office: ACTION EUR
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 7
Previous Channel Indicators: n/a
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 19-Oct-2004 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 2966600
Secure: OPEN
Status: NATIVE
Subject: MAJOR FISCAL ELEMENTS IN THE CHANCELLOR'S MARCH 29 BUDGET UNCLASSIFIED
TAGS: ECON, UK
To: STATE TRSY
Type: TE
vdkgvkey: odbc://SAS/SAS.dbo.SAS_Docs/ceaa01b0-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009